The EITC and the Taxation of Lower-Income Working Families

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I. INTRODUCTION

An important concern for federal policymakers is determining the appropriate level and structure of taxes on lower-income families. While average tax rates on families with modest incomes are low, tax system complexities and high marginal tax rates create problems for lower-income families, just as they do for families at middle and higher income levels.

The largest tax burden faced by lower-income working families is the federal payroll tax which supports Social Security and Medicare. The payroll tax rate has risen from 9.6 percent in 1970, to 15.3 percent today - a 59 percent increase. Concerns about the high level of payroll taxes contributed to the 1975 enactment, and later expansions, of the earned income tax credit (EITC). The EITC allows millions of families to eliminate their federal income tax liability, and because it is a refundable credit, gives families a cash payment to offset the high payroll tax burden.

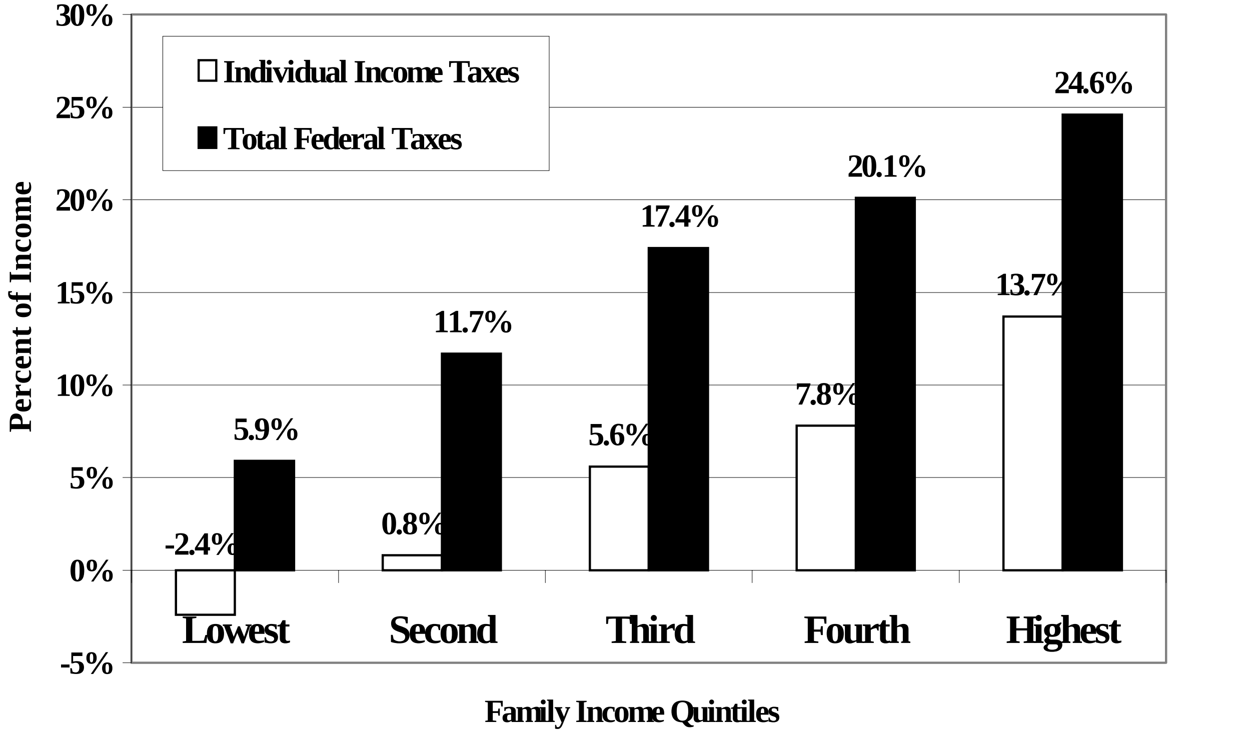
The EITC is available to families who have earnings from employment, and may be claimed both by families with and without children. The estimated budget cost of the EITC for fiscal 2000 is $29.8 billion, of which $25.8 billion (87 percent) represents budget outlays for the refundable portion of the credit.

This paper examines federal taxes on lower-income families with a focus on the EITC because of its central role in low-income tax policy. The structure, rationale, growth, and problems with the EITC are discussed. These problems include the EITC's complexity, its high level of error and fraud, the marriage penalty created by the EITC, and the high marginal tax rates imposed on families in the EITC's "phase-out" range. The concluding section looks at some recent proposals to change tax provisions affecting lower-income families.

II. FEDERAL TAXES ON LOWER-INCOME FAMILIES

The federal tax system is highly progressive. This means that families at lower income levels pay substantially smaller shares of their income towards taxes than do higher-income families. Figure 1 shows Department of Treasury estimates of average tax burdens for U.S. families grouped into five income groups, or "quintiles," for 2000.[1] The average family in the highest income quintile (those with incomes above $100,767) will pay 24.6 percent of their income towards federal taxes this year.[2] Families in the bottom quintile (those with incomes below $17,988) will pay 5.9 percent of their income towards taxes, on average. A "family" refers to either a single individual, a single head of a household with children, or a married couple.

Figure 1: Average Federal Taxes as a Percent of Income, by Family Income Quintile, Estimated 2000



Note: Income quintiles begin at incomes of: $0, $17,988, $34,844, $59,019, and $100,767.
Source: Department of Treasury. Estimates based on "Family Economic Income," which is a very broad measure of income.

It is important to keep in mind that each quintile in Figure 1 contains some 23 million families, many of which are in quite different positions in life. In particular, retirees in the bottom two quintiles whose main source of income is Social Security may pay little individual income or payroll taxes. But these lower quintiles also contain millions of working families who pay a steep 15.3 percent payroll tax on all wages up to $76,200 to fund the Social Security and Medicare programs.

In fact, payroll taxes are by far the largest federal tax burden on lower-income families, accounting for 81 percent of post-EITC taxes for families in the lowest two quintiles (those with incomes under $34,844). Federal excise taxes on cigarettes, gasoline, and other products may also impose a substantial burden on lower-income families, depending of course on individual lifestyle. A two-pack a day smoker earning $20,000 per year pays about 1.2 percent of her gross income towards federal cigarette taxes, with a further increase scheduled for 2002 under current law.[3] Treasury estimates show that corporate income taxes also impose a burden on lower-income families. For example, retirees receiving income from savings and pensions pay a hidden amount of corporate-level tax.[4]

Most lower-income families do not pay personal income taxes. Figure 1 showed that, averaging across families, the lowest income quintile had a negative income tax rate. This occurs because positive tax payments by some lower-income families are more than offset by refundable EITC payments to other families.

The income tax code contains numerous provisions to shield lower-income families from tax, including the standard deduction and the personal exemption. This year, the standard deduction is $7,350 for married couples, and the personal exemption is $2,800. As a result, a married couple with no children will not pay income tax on at least the first $12,950 of income in 2000 (see Table 1). The $500 child tax credit, substantially increases this income tax threshold, or "tax-entry point," for families with children. Table 1 shows that the income tax threshold for a family of four taking two child credits is $25,217 in 2000.

Table 1: Income Tax Thresholds, 2000
(Excluding EITC)

Family Type	Single	Married
No children	$7,200	$12,950
One child	$15,383	$19,083
Two children	$21,517	$25,217

Note: includes effect of standard deduction, personal exemptions, and child tax credit.
Source: Joint Economic Committee calculations.

For families that are eligible for the EITC, income tax thresholds are even higher. As discussed in Section III, lower-income families with earnings from work may take the EITC, which provides benefits that vary depending on income level and number of children. Table 2 shows income tax thresholds assuming that both the child tax credit and the EITC are taken. For example, a family of four could earn up to $28,682 this year without paying any income taxes.

Table 2: Income Tax Thresholds, 2000
(Including EITC)

Family Type	Single	Married
No children	$8,274	$12,950
One child	$21,588	$23,380
Two children	$27,144	$28,682

Note: includes effect of standard deduction, personal exemptions, child tax credit, and EITC. Assumes all income is earned income.
Source: Joint Economic Committee calculations.

A primary rationale for exemption of a substantial amount of income from taxation is to prevent the government from taxing families into poverty. The income tax system currently meets this goal. The Committee on Ways and Means estimates that in 2000 a family of four will have an income tax threshold 48 percent above the poverty level.[5] There has been a steady improvement in the income tax position of lower-income families since the 1980s. Back in 1984, the income tax threshold for a family of four was 17 percent below the poverty level. Some of the changes that have boosted the income tax position of lower-income families include tax code inflation indexing, increases in the standard deduction and personal exemption amounts under the Tax Reform Act of 1986 (TRA86), EITC benefit increases in 1986, 1990, and 1993, and the $500 child tax credit enacted in 1997.

As a result of these changes, an increasing share of U.S. families do not owe personal income tax. Table 3 shows Joint Committee on Taxation (JCT) estimates for the percent of families at different income levels who pay some federal income tax.[6] At income levels above $50,000, more than 98 percent of families pay tax. At lower income levels, much smaller percentages of families pay tax. In total, JCT figures show that just 64 percent of U.S. families paid income tax in 1999, down from about 73 percent in the early 1990s. Therefore, 36 percent, or 49 million families, did not pay income tax in 1999.

Table 3: Share of Familes Paying Income Tax, 1999

Income Group (000s)	Share
<$10,000	6.5%
$10-$20	32.8%
$20-$30	64.3%
$30-$40	85.1%
$40-$50	93.5%
$50-$75	98.5%
$75-$100	99.5%
$100-$200	99.9%
$200+	99.9%
Total	64.4%

Source: JEC based on JCT figures.

Parallel to the declining share of families that pay tax, is a fall in the average income tax rate on lower-income families. Treasury calculations, which show the average tax rate on a family with half the median income, indicate a steady decline since the 1980s.[7] Similarly, IRS figures (which are on a pre-refundable EITC basis) show that the average income tax rate on the bottom 50 percent of tax filers has declined since the 1980s. The average tax rate on this group fell from 5.1 percent in 1987 to 4.5 percent by 1997. New preliminary IRS data shows that the average tax rate on lower-income families fell further in 1998.[8] This was the first year that the new child tax credit was effective.

III. STRUCTURE OF THE EITC

The expansion of the EITC over time has played an important role in the reduction of taxes on lower-income families. The EITC started out as a small, temporary 10-percent credit in 1975 with a maximum value of $400. After being made permanent in 1978, the EITC was expanded substantially in 1986, 1990, and 1993.[9] Today it is a much larger program with credit rates up to 40 percent, and a maximum credit of $3,888. Table 4 briefly summarizes the legislative history of the credit.

Table 4: EITC Brief Legislative History

Year	Changes
1975	Enactment of a 10% refundable credit (same rate for all families with children).
1986	Indexed for inflation; maximum credit increased; eligible income range expanded.
1990	Expanded credit for 2+ children; phased-in credit rate increases.
1993	Credit added for families with no children; phased-in credit rate increases to 7.65% (no kids), 34% (1 kid), and 40% (2+ kids).

Source: Joint Economic Committee.

Table 5 summarizes EITC parameters for 2000.[10] The maximum EITC amounts for this year are: $3,888 for a family with two or more children, $2,353 for a family with one child, and $353 for a family with no children. For families with incomes above the beginning of the phase-out ranges shown, the allowable credit is reduced by the phase-out rate.

Table 5: EITC for 2000

EITC Item	No Children	One Child	Two or More Children
Credit rate	7.65%	34%	40%
Phase-out rate	7.65%	15.98%	21.06%
Maximum credit	$353	$2,353	$3,888
Phase-out income range	$5,770-$10,380	$12,690-$27,413	$12,690-$31,152

Source: Congressional Research Service.

Most of the EITC budget cost stems from the fact that it is a refundable credit. This means that families receiving the EITC that have no income tax liability may receive a cash payment from the Treasury, which for budget purposes is counted as an outlay. For example, a family which owed $500 in income taxes before counting EITC, and had a $2,000 EITC, would receive a $1,500 check from the Treasury.

Over time, the EITC has become less of a tax reduction program, and more of a cash transfer program. The refundable or budget outlay portion of the EITC has risen from 70 percent in 1990 to an estimated 87 percent in 2000. Table 6 summarizes the components of the EITC for fiscal year 2000.

Table 6: Components of the EITC, Estimated Fiscal Year 2000

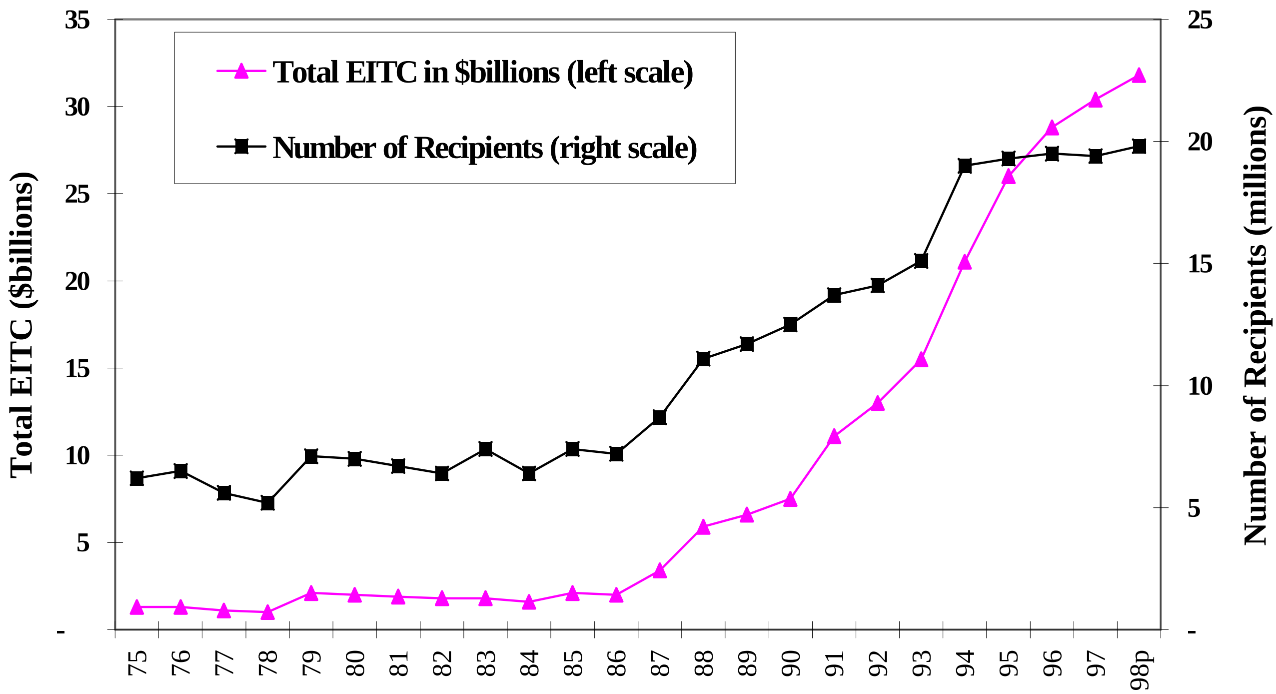
Budget Cost	Cost Share	Item
$4.0	13%	Tax reduction
$25.8	87%	Budget outlay
$29.8	100%	Total budget cost

Source: Joint Committee on Taxation.

IV. RATIONALES FOR THE EITC

The EITC has enjoyed substantial support since its inception based on three main rationales. First, the program is supported as an anti-poverty mechanism which redistributes resources to lower-income working families. Total resources transferred through the program have grown substantially, as measured by dollars or recipients. Figure 2 shows that the number of EITC recipients rose from 7.2 million in 1986, to 19.8 million in 1998. During the same period, total EITC claimed rose from $2.0 billion to $31.8 billion, according to preliminary IRS figures for 1998. (Current JCT estimates for the EITC's cost are somewhat lower, and are likely to be revised upward to take into account the new IRS data).

Figure 2: Total EITC and Number of Recipients



Source: IRS. IRS values for 1998 are preliminary.

A second goal of the EITC is to provide an offset to the heavy payroll tax burden on lower-income working families. While this burden is real, Social Security payroll taxes are supposed to be something akin to pension plan contributions. These contributions entitle lower-income families to Social Security benefits which are built on a structure that redistributes income in their favor. This suggests that the goal of offsetting payroll tax for lower-income families does not rest on strong theoretical foundations.

Nonetheless, the 15.3-percent federal payroll tax does create a substantial burden since it has no deductions from the base so that the tax starts at the first dollar earned. As a result, the payroll tax burden is larger than the income tax burden for about 80 percent of working families.[11] The refundable portion of the EITC helps families offset this burden.

This goal of the EITC highlights a general problem with the federal tax code. Namely that much complexity is generated by new tax provisions which are added to the code in order to simply offset existing tax code problems. In this case, the steadily increasing payroll tax burden from the 1960s to the 1980s prompted the enactment and expansion of the complex EITC system to counteract the rising burden on lower-income families.

Increases in the excise tax burden have also prompted lawmakers to seek higher EITC benefits. For example, the 1990 EITC increase was partly prompted by that year's excise tax increase.[12] And in 1993, President Clinton's EITC expansion was also partly premised on the need to offset the negative impact of the Administration's excise tax increases.[13]

The third goal of the EITC is to provide a work incentive for individuals who may otherwise support their families on government transfer payments or other means. Concern regarding the disincentives to work built into the U.S. welfare system in the early 1970s were an important factor in gaining support for the EITC's enactment in 1975. Again, this illustrates how the EITC has gained support as an offset to the negative effects of other government programs.

The goal of creating a wage subsidy to encourage work has attracted broad bipartisan support for the EITC over the years. Evidence indicates that the credit provides a modest stimulus to increasing labor force participation for lower-income families.[14] However, as discussed in the next section, this positive work incentive for some individuals is offset by a negative work incentive for other families. EITC recipients in the phase-out range of the credit face a high effective marginal tax rate because more work reduces EITC benefits in this income range. As a result, the overall work incentive effect of the EITC is mixed – some individuals may be encouraged to enter the labor force, but others are discouraged from earning additional income for fear of losing EITC payments.

V. PROBLEMS WITH THE EITC

High Marginal Tax Rates

In Section II, data was presented showing that <u>average</u> tax rates for lower-income families are low. But tax policy must also consider <u>marginal</u> tax rates because they create incentives and disincentives that can have substantial effects on the economy. Effective marginal tax rates measure the additional taxes a family would pay if they earned an additional dollar of income. If marginal tax rates on earnings are too high, they create a disincentive to work, or to take the steps necessary to gain a higher-paying job.

Three main features of the federal tax code can create high marginal tax rates on labor earnings of lower-income families. First, the combined Social Security and Medicare payroll tax begins at the first dollar of earned income for every working family. While half of the tax (7.65 percent) is nominally paid by employers, economists agree that the tax is actually borne by workers, and effectively reduces the gross amount seen by workers on their paystubs.[15]

Second, the 15-percent bottom income tax rate generally becomes effective above the income level determined by the sum of personal exemptions and the standard deduction (low-income families generally do not itemize deductions). For example, a married couple with no children face a combined income and payroll tax rate of 28.1 percent beginning at $12,950 of wage income in 2000. (The rate is calculated as (15.3 + 15) / 1.0765 to take into account the 7.65 percent "employer" half of the payroll tax which represents further income that is immediately taxed away).

Third, the EITC phase-out rate can add to the income and payroll tax rates to create a very high marginal tax rate for lower-income working families. The EITC has three different phase-out rates depending on the number of children claimed, as shown in row 2 of Table 7. The phase-out rate acts like a marginal tax rate because it partly offsets any wage increase that a worker may receive. Numerous provisions in the income tax code have phase-outs that boost marginal tax rates, but the EITC phase-out rates are particularly high. For example, the child tax credit phases-out at just 5 percent, compared to the highest 21-percent rate for the EITC.[16]

Table 7: Marginal Income Tax Rates on Families Within the EITC Phase-Out Range

Item	No Children	One Child	Two Children
EITC phase-out range	$5,770-$10,380	$12,690-$27,413	$12,690-$31,152
1. Income tax rate	15%	15%	15%
2. EITC phase-out rate	7.65%	15.98%	21.06%
Tax rate (1+2)	22.65%	30.98%	36.06%
3. Payroll tax rate	15.3%	15.3%	15.3%
Total tax rate (1+2+3)	**35.3%**	**43.0%**	**47.7%**

Note: the 15% marginal income tax rate (line 1) may not affect some families when the child tax credit reduces income tax liability to zero.
Source: Joint Economic Committee.

Consider a married couple with two children earning $28,000 who receive a $1,000 raise. The raise first incurs $153 in federal payroll tax liability, followed by a $150 federal income tax liability. Then, the family's higher income will mean that its EITC will be cut by $210 since it phases-out at 21 percent. In total, the $1,000 raise would be counter-balanced by a $513 increase in taxes and reduction in EITC benefits. The effective marginal tax rate on the family is 47.7 percent ($513 / $1,076.5). With the additional of state income taxes, the marginal tax rate for this family earning a modest income will be about 50 percent.

This high marginal tax rate can be a problem for millions of lower-income taxpayers because the EITC phase-out range is broad. For families with two or more children it stretches from $12,690 to $31,152 in 2000. Over half of EITC claimants, an estimated 10.5 million in 1999, are in the phase-out range and therefore may be subject to the high marginal rate created by the credit.[17]

One factor which does, however, mitigate the high tax rates created by the EITC phase-out is the $500 child tax credit. For certain income ranges, the child tax credit zeros out income tax liability for many lower-income families. This has the effect of eliminating the 15-percent income tax rate for families at certain income levels within the broad EITC phase-out ranges.

The EITC phase-out does fulfill an important policy goal of limiting the program's benefits to those most in need. But as the EITC program has grown and benefits have become more generous, a faster phase-out rate has become mathematically necessary if the credit is to remain targeted below certain income levels. In fact, the highest phase-out rate today of 21.06 percent is up from just 10 percent when the EITC was created in 1975. This factor poses a significant hurdle to future considerations of EITC benefit increases.

Marriage Penalties

Substantial concern has been expressed in recent years regarding features of the income tax code which create "marriage penalties." These occur when a married couple pays more in income tax by filing jointly, than they would in sum if they divorced and filed separately. Marriage penalties are mainly caused by the breakpoints between tax brackets for married taxpayers (which are not twice the breakpoints for single taxpayers), and the standard deduction for married taxpayers (which is not twice that for single taxpayers).

In addition, lower-income families face marriage penalties in the tax code from two features of the EITC. First, the income range of the EITC phase-out is the same for singles and married filers so that a two-earner married couple would lose some or all of the EITC they could take as singles because of their higher combined income. For example, two singles earning $20,000 each could claim the EITC separately, but if they married they could not because their combined income would be too high. Second, the EITC does not increase for taxpayers with more than two children. Two singles each having children who get married may not be able to claim the credit for children they previously claimed for, or the amount claimed may be less.

A recent Treasury report estimated that in 1999, 28 percent of married couples with income between $0 and $30,000 had a marriage penalty.[18] Marriage penalties for these families could be reduced by increasing the standard deduction, increasing the EITC for two-earner married couples, and increasing the EITC for couples with more than two children.

Complexity

Annual reviews by the IRS National Taxpayer Advocate in 1998 and 1999 found that the EITC was the third "most serious problem facing taxpayers."[19] The Advocate found that the tax law regarding the EITC was complex, and that because it is a refundable credit, taxpayers were too eager to claim the credit without understanding whether they are actually eligible.

Like many parts of the tax code, the EITC's complexity stems both from lawmakers' attempts to create tax provisions that are fair, and to their efforts to limit revenue losses to the budget. To limit revenue losses, the EITC phases-out as income rises. Phase-out calculations are typically complex, and make it so that recipients don't know how much their tax benefits will be before filling in their tax forms. Other EITC complicating factors include the determination of whether or not a child is eligible, earned income and modified adjusted gross income calculations, and the disqualified income calculation. In the pursuit of fairness, the EITC incorporates three separate credit rates, phase-out rates, and phase-out ranges for families with different numbers of children.

All in all, these and other rules make the EITC complicated enough that about half of EITC recipients use tax return preparers instead of completing the return by themselves, according to the General Accounting Office (GAO).[20] Other than the EITC, tax professionals have identified a diverse range of tax complexities faced by lower-income families. These include dependency exemptions, education expense deductions, tip income, filing status issues, self-employment income, alimony and child support, pension income, dependent care credits, unemployment compensation, disability income, the child credit, and the tuition credit.[21] For example, the dependent care credit overlaps the EITC in terms of eligibility, perhaps causing confusion on the part of some families. And the partial phase-out range of the dependent care credit overlaps the EITC phase-out range, and boosts the marginal tax rate on lower-income recipient families by another 2.4 percent.

High Error and Fraud Rate

The EITC is a unique part of the federal tax code. As a refundable credit, the EITC delivers cash payments to over 15 million families who pay no federal income taxes. Unfortunately, the prospect of receiving cash handouts from the Treasury has led to a high fraud rate in the program as tax filers have claimed excessive refunds for which they are not due. And the complexity of the credit has led to high error rates as tax filers have difficulty figuring out such factors as which children can be claimed and what types of income need to be taken into account for tax calculations.

Concerns about the high error and fraud rates led to investigations in the mid-1990s by the IRS and the GAO. A 1997 IRS study based on 1994 returns found that on total EITC claims of $17.2 billion, $4.4 billion was in excess, or 26 percent of the total. This very high EITC overcharge rate was consistent with earlier IRS studies.[22] In 1998, the General Accounting Office (GAO) examined the IRS analysis and found it to be reasonably accurate.[23]

EITC overcharging problems stem from filing status claims, over-reporting income to garner a larger credit, and claims for ineligible or fictitious children (two-thirds of the $4.4 billion overcharge in 1994 related to qualifying children issues). Part of the problem has been that unscrupulous tax preparers have preyed on unsuspecting workers, including immigrants for whom English is not a first language. For a fee, workers are promised loans in anticipation of EITC refunds from tax preparers who help them fill out false returns.

Legislative and procedural changes at the IRS since the mid-1990s have led to better enforcement of the EITC program. For example, since 1995 the IRS validates Social Security numbers of all claimants. And the 1997 Taxpayer Relief Act added additional penalties on taxpayers who fraudulently claim credits for which they are not eligible, and added due diligence requirements for tax preparers regarding the EITC. A recent GAO report on last year's IRS filing season did indicate that new IRS procedures were stopping millions of dollars of false EITC claims.[24]

However, the EITC error and fraud rate can probably be only reduced so far. The types of noncompliance found in the EITC program are not items that are easy for the IRS to verify. The IRS was not set up to do the type of enforcement that such a program really needs, and full compliance is a costly and time-consuming proposition.

Certainly, other parts of the income tax code are complex, and have substantial error rates and enforcement costs. The EITC does illustrate the general problem with the creation of special incentives and subsidies in the tax code. These create real headaches and costs for both taxpayers and government administrators. The IRS now spends over $140 million per year on EITC compliance.[25] As mentioned, half of EITC recipients use tax preparers, and there are indications that new IRS compliance procedures for the EITC may be so burdensome that some eligible taxpayers aren't bothering with the credit any longer.

VI. CONCLUSIONS AND PROPOSALS FOR CHANGE

This paper discussed taxation of lower-income families with a focus on the EITC because of its growing role in federal tax policy. A number of recent tax proposals would increase the after-tax income of lower-income families by increasing the EITC, cutting income tax rates, or increasing the child tax credit. Other proposals have been suggested in recent years to simplify and rationalize tax policy for families at modest income levels.

Following are brief summaries of some recent proposals and ideas for reform:

- **EITC Expansion**. The Administration's fiscal 2001 budget proposes to increase the EITC credit for families with three or more children, reduce the EITC marriage penalty by raising the phase-out threshold for two-earner couples, and provide other minor EITC adjustments. The House of Representatives has passed, and the Senate is expected to pass, a broad marriage penalty relief bill which would reduce the marriage penalty for EITC recipients by raising the income phase-out range for claimants. Vice President Al Gore also proposes to reduce the marriage penalty for EITC recipients.

- **Reduce Marginal Tax Rates**. As discussed, working families with modest incomes may face high marginal tax rates. Governor George Bush's tax plan would lower tax rates on these families in two ways. First, the bottom income tax rate would fall to 10 percent, compared to 15 percent under current law. This would lower taxes, or increase EITC refunds, for millions of families. Second, the plan would double the child tax credit to provide a tax cut for millions of families with children. It would also reduce the marginal tax rate for many families, including many in the high tax rate EITC phase-out range. This occurs because the child tax credit nullifies the effect of the 15-percent income tax rate for families over a broad income range.

- **Payroll Tax Reduction**. The tax system could be simplified by replacing the EITC with a payroll tax exemption for wage levels below the poverty line. Since the EITC is designed to counteract high payroll taxes, this approach would accomplish that goal more directly. In addition, this change would eliminate the high marginal tax rate of the EITC phase-out range, eliminate the problem of EITC fraud, and reduce the number of families filing income tax returns. Reductions in the payroll tax may, alternatively, be realized through Social Security reforms which would convert payroll taxes into private pension plan contributions.

- **Integration of Low-Income Tax Benefits.** To simplify the income tax code, some of the numerous provisions designed to reduce taxes on the poor could be consolidated into a single credit or exemption. For example, some analysts have suggested rolling together the dependency exemption and the child tax credit. Alternatively, various Flat Tax proposals would eliminate all credits and deductions and replace them with a single very large income exemption.

Tax proposals affecting lower-income families should be considered in light of the various tax implications discussed here. Would policy changes simplify, or further complicate, the tax code for lower-income families? How are the high marginal tax rates under the EITC phase-out affected? Would changes affect the number of families required to pay income tax? Are marriage penalties increased or reduced? The tax system can place unintended roadblocks in front of families at all income levels, so everyone has a stake in proposals designed to lower tax rates and simplify the income tax structure.

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[1] *U.S. Treasury Distributional Analysis Methodology*, OTA Paper 85, Julie-Anne Cronin, U.S. Department of Treasury, September 1999.
[2] It should be noted that distributional charts should be used with caution, as they are based on numerous measurements and assumptions. For example, these measurements are based on Treasury's measure of "Family Economic Income" which can differ substantially from other more familiar definitions of income such adjusted gross income (AGI) under the federal income tax.
[3] The 2000 federal cigarette tax is 34 cents, and scheduled to rise to 39 cents in 2002 under the Balanced Budget Act of 1997. This does not include costs from any federal or state tobacco litigation settlement, or any other current proposals.
[4] The Treasury currently assumes that the burden of the corporate income tax falls on the owners of capital. (The JCT currently does not distribute the corporate income tax due to uncertainty regarding the incidence).
[5] *1998 Green Book*, Committee on Ways and Means, May 19, 1998. The estimate for 2000 may be slightly off now since it is was completed in 1998.
[6] *Estimates of Federal Tax Expenditures for Fiscal Years 2000-2004*, Joint Committee on Taxation, December 22, 1999. JCT figures include families that file returns and some types of non-filing families. As a result, they capture a larger universe of families than do IRS statistics which just include families that file returns.
[7] *Average and Marginal Federal Income, Social Security and Medicare, and Combined Tax Rates for Four-Person Families at the Same Relative Positions in the Income Distribution, 1955-1999*, Allen Lerman, U.S. Treasury, January 15, 1998
[8] *SOI Bulletin*, IRS, Spring 1999. And e-mail received from the Statistics of Income Division, IRS, February 2000.
[9] The 1975 law enacted the EITC temporarily. The credit was enacted permanently in 1978.
[10] *The Earned Income Credit: Benefit Amounts*, Melinda Gish, Congressional Research Service, January 2000.
[11] *Estimates of Federal Tax Liabilities for Individuals and Families by Income Category and Family Type for 1995 and 1996*, Congressional Budget Office, May 1998.
[12] See "A Choice for Choices: Tax Incentives and Cultural Preference," Karen Yeager in *Tax Notes*, April 20, 1998.

[13] *The Earned Income Tax Credit: A Growing Form of Aid to Low-Income Workers*, James Storey, Congressional Research Service, December 5, 1996.

[14] The EITC creates a range of incentive effects for individuals at different income levels and family situations. Like changes in wages, the EITC creates both "income" and "substitution" effects on labor supply decisions which may produce opposite incentive effects. See *The Earned Income Tax Credit (EITC): Effects on Work Effort*, Jane Gravelle, Congressional Research Service, August 30, 1995. See *also The Earned Income Tax Credit: An Invisible Welfare Program*, Naomi Lopez, Institute for Policy Innovation, 2000.

[15] *Present Law and Analysis Related to Individual Effective Marginal Tax Rates*, Joint Committee on Taxation, February 3, 1998.

[16] See *Present Law and Analysis Relating to Individual Effective Marginal Tax Rates*, Joint Committee on Taxation, February 3, 1998.

[17] *Overview of Present Law and Issues Relating to Individual Income Taxes*, Joint Committee on Taxation, April 14, 1999.

[18] *Defining and Measuring Marriage Penalties and Bonuses*, Nicholas Bull, Janet Holtzblatt, James Nunns, and Robert Rebelein, Office of Tax Analysis Paper 82, U.S. Treasury, November 1999.

[19] *Annual Report to Congress*, National Taxpayer Advocate, Internal Revenue Service, FY 1999.

[20] *Earned Income Credit: IRS' Tax Year 1994 Compliance Study and Recent Efforts to Reduce Noncompliance*, General Accounting Office, July 1998.

[21] "Tax Controversy Among the Low-Income Population," *Tax Notes*, Eugene Steuerle, May 17, 1999.

[22] Reforming the Earned Income Credit Program, George Yin in *Tax Notes*, June 26, 1995.

[23] *Earned Income Credit: IRS' Tax Year 1994 Compliance Study and Recent Efforts to Reduce Noncompliance*, General Accounting Office, July 1998.

[24] *Tax Administration: IRS 99' Tax Filing Season*, General Accounting Office, December 1999.

[25] *Budget of the United States Government*, *Appendix*, Fiscal Year 2001.